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UNITED STATES TELEPHONE ASSOCIATION

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March 20,1997

Mr. William F. Caton
Secretary
Federal Communications Commission
1919 M Street, N.W., Room 222
Washington, D.C. 20554

Re: Ex Parte
CC Docket No.96-262

Dear Mr. Caton:

On Thursday, March 20, 1996, USTA representatives Maureen Keenan of Bell Atlantic, Jeff Pursley of Aliant Communications, and Frank McKennedy of USTA, met with Commission Staff members Rich Lerner, Steve Spaeth, Jeff Lanning and John Scott.

The purpose of the meeting was to discuss the USTA proposal in this proceeding for a simplified price cap basket structure and how USTA's proposed simplified price cap formula produces results that are identical to the original formula under today's price cap basket structure or USTA's simplified basket proposal. USTA also discussed a change in the price cap formula "R" component to an "RCAP" component which would eliminate the anomalous price cap index results that occur when exogenous changes are incorporated in the formula.

The original and a copy of this letter, and, at the request of the Commission staff, materials depicting the streamlined price cap structure, the proposed price cap formula adjustments and draft Part 61 rules changes along with a machine readable disk of the supporting spread sheets are being filed in the office of the Secretary today. Please include this material in the record of the above reference proceeding.

Respectfully submitted,

Frank McKennedy
Director - Legal and Regulatory Affairs

cc with attach: Jeff Lanning
Rich Lerner
John Scott
Steve Spaeth

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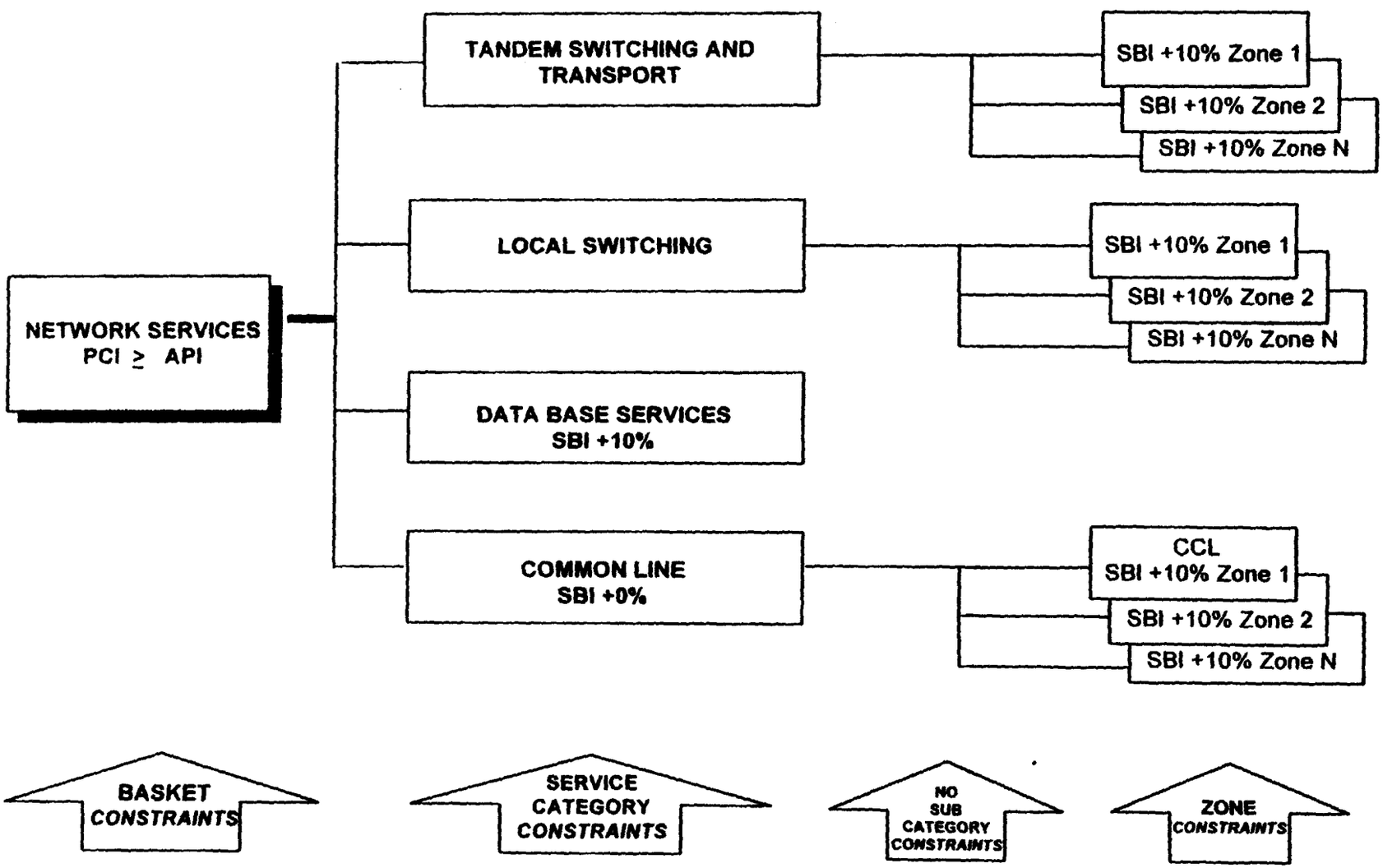
PROPOSED LEC PRICE CAP STRUCTURE



ATTACHMENT 9

USTA
PROPOSED LEC PRICE CAP STRUCTURE

USTA COMMENTS
CC DOCKET NO. 96-262
JANUARY 29, 1997

CHART 3

No Additional Headroom is created when the 3 Existing Access Baskets are put into 1 Basket as Service Categories

Ln#	Description	Abbrev.	Source	Access Services	Common Line	Traffic Sensitive	Trunking
3.01	Proposed Max Revenue		Chart 2, Ln 2.13	32,109,866			
			Calculation of Basket PCI and Max Revenue				
3.02	Existing PCI	PCI(t-1)	Initialized @ 100%	100.0000%			
3.03	Existing API	API(t-1)	Calculated based on Total Headroom	99.3194%			
3.04	GDP-PI	GDPPI	1996 Annual Filing	2.6514%			
3.05	X-Factor	X	1996 Annual Filing	5.3%			
3.06	Delta Z	Z	Sum of all 1996 Access Exogenous Costs	1,082,964			
3.07	RCAP	RCAP	Chart 2, Ln 2.04	31,900,502			
3.08	Proposed PCI	PCI(t)	PCI(t-1) * [1+ GDPPI - X] * [1 + Z/RCAP]	100.6563%			
3.09	Existing Revenue	R(t-1)	Sum of all R(t-1) values	31,683,392			
3.10	Proposed Max Revenue		[PCI(t) / API(t-1)] * R(t-1)	32,109,866			
			Calculation of Service Category SBI Limits and Max Revenue				
3.11	Existing SBI Limit	SBILimit(t-1)	1996 Annual Filing Proposed PCIs		93.7772%	85.1215%	85.9023%
3.12	Existing SBI	SBI(t-1)	1996 Annual Filing Proposed APIs		93.7772%	83.3292%	85.7651%
3.13	GDP-PI	GDPPI	1996 Annual Filing		2.6514%	2.6514%	2.6514%
3.14	X-Factor	X	1996 Annual Filing		5.3%	5.3%	5.3%
3.15	Delta Z	Z	1996 Annual Filing		467,000	293,396	322,568
3.16	RCAP	RCAP(t-1)	Chart 2, Ln 2.04	31,900,502	11,786,072	9,506,514	10,607,916
3.17	Proposed SBI Limit	SBILimit(t)	SBILimit(t-1) * [1+ GDPPI - X] * [1 + Z/RCAP] * 1.00		94.9107%	85.4245%	86.1700%
3.18	Existing Revenue	R(t-1)	1996 Annual Filing		11,786,072	9,306,347	10,590,973
3.19	Proposed Max Revenue		[SBILimit(t) / SBI(t-1)] * R(t-1)	32,109,866	11,928,537	9,540,350	10,640,979

Chart 4

- Demonstration of USTA's basket and service category proposal.
  - Shows USTA's proposed pricing flexibility.
  - Price cap companies need this limited pricing flexibility.
- Service categories are restrained by an overall cap at the basket level.
- Common Line sub-categories are restrained by an overall cap at the Common Line service category level.

CHART 4

USTA's Basket and Bands Proposal

Calculation of Basket PCI and Max Revenue

Ln#	Description	Acc Svcs
4.01	Existing Revenue	31,683,392
4.02	Existing PCI	100.0000%
4.03	Existing API	99.3194%
4.04	GDP-PI	2.6514%
4.05	X-Factor	5.3%
4.06	Delta Z	1,082,964
4.07	RCAP	31,900,502
4.08	Proposed PCI	100.6563%
4.09	Proposed Max Revenue	32,109,866

Calculation of Service Category SBI Limits and Max Revenue

		Comm Line	LS - 1	LS - 2	LS - n	T&TS - 1	T&TS - 2	T&TS - n	DB & Other	Overall
4.10	Existing Revenue	11,786,072	2,312,833	2,763,600	3,850,647	2,743,916	3,278,699	4,568,358	379,267	
4.11	Existing SBI Limit	93.7772%	85.1215%	85.1215%	85.1215%	85.9023%	85.9023%	85.9023%	85.1215%	
4.12	Existing SBI	93.7772%	83.3292%	83.3292%	83.3292%	85.7651%	85.7651%	85.7651%	83.3292%	
4.13	GDP-PI	2.6514%	2.6514%	2.6514%	2.6514%	2.6514%	2.6514%	2.6514%	2.6514%	
4.14	X-Factor	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	
4.15	Delta Z	467,000	72,915	87,126	121,397	83,571	99,859	139,138	11,957	
4.16	RCAP	11,866,836	2,328,682	2,782,537	3,877,033	2,762,718	3,301,166	4,599,663	381,866	
4.17	Flexibility	0%	10%	10%	10%	10%	10%	10%	10%	
4.18	Proposed SBI Limit	94.8861%	94.0079%	94.0079%	94.0079%	94.7725%	94.7725%	94.7725%	94.0079%	
4.19	Proposed Max Revenue	11,925,443	2,609,224	3,117,756	4,344,109	3,032,092	3,623,040	5,048,143	427,870	32,109,866

Calculation of Sub-Index SBI Limits and Max Revenue

		CL - 1	CL - 2	CL - n	Overall
4.20	Existing Revenue	3,053,543	3,648,672	5,083,858	
4.21	Existing SBI Limit	93.7772%	93.7772%	93.7772%	
4.22	Existing SBI	93.7772%	93.7772%	93.7772%	
4.23	GDP-PI	2.6514%	2.6514%	2.6514%	
4.24	X-Factor	5.3%	5.3%	5.3%	
4.25	Delta Z	120,991	144,571	201,438	
4.26	RCAP	3,074,467	3,673,674	5,118,695	
4.27	Flexibility	10%	10%	10%	
4.28	Proposed SBI Limit	104.3747%	104.3747%	104.3747%	
4.29	Proposed Max Revenue	3,398,616	4,060,999	5,658,372	11,925,443

§ 61.42 Price cap baskets and service categories

(d) Each local exchange carrier subject to price cap regulation shall establish a basket of services for interstate access elements.

(e) The interstate access basket shall contain such services as the Commission shall permit or require, including the following service categories:

(1) Common line as described in §§ 69.103, 69.104, 69.105, and 69.115 of this chapter;

(2) Local switching density zones including services as described in §§ 69.106 and 69.109 of this chapter;

(3) Transport and tandem switching density zones including services as described in §§ 69.110, 69.111, 69.112, 69.114, 69.124, and 69.125 of this chapter; and

(4) Database and other including database access services and services described in § 69.128 of this chapter.

(f) The common line service category shall contain density zone subcategories.

§ 61.45 Adjustments to the PCI for local exchange carriers

(b) Notwithstanding the value of X defined in § 61.44(b), the X value applicable to the basket specified in § 61.42(d) shall be 4.0%, or 4.7%, or 5.3%, as the carrier elects.

(c) Adjustments to local exchange carrier PCIs for the basket designated in § 61.42(d) shall be made pursuant to the following formula:

$$PCI_t = PCI_{t-1} * (1 + \Delta Z/RCAP) * (1 + GDP\text{-}PI - X)$$

where

PCI_t = the new PCI value,
PCI_{t-1} = the immediately preceding PCI value,
ΔZ = the dollar effect of current regulatory changes when compared to the regulations in effect at the time the PCI was updated to PCI_{t-1}, measured at base period level of operations,
RCAP = $(PCI_{t-1} / API_{t-1}) * R_{t-1}$,
API_{t-1} = the existing API value,
R_{t-1} = base period quantities for each rate element "i", multiplied by the existing price for each rate element "i",
GDP-PI = the percentage change in the GDP-PI between the quarter ending six months prior to the effective date of the new annual tariff and the corresponding quarter of the previous year, and
X = productivity factor of 4.0%, or 4.7%, or 5.3% is the carrier so elects.

§ 61.46 Adjustments to the API

(a) In connection with any price cap tariff filing proposing rate changes, the carrier must calculate an API for each affected basket pursuant to the following methodology:

$$API_t = API_{t-1} * ([\Sigma_1(p_t * d)i] / [\Sigma_1(p_{t-1} * d)i])$$

where

API_t = the proposed API value,
API_{t-1} = the existing API value,
p_t = the proposed price for rate element "i",
p_{t-1} = the existing price for rate element "i", and
d = the base period demand for rate element "i".

§ 61.47 Adjustments to the SBI Limits; SBIs

(a) In connection with any price cap tariff filing proposing change in the rates of service categories or subcategories, the carrier must calculate an SBI value for each affected service category or subcategory pursuant to the following methodology:

$$SBI_t = SBI_{t-1} * ([\Sigma_1(p_t * d)i] / [\Sigma_1(p_{t-1} * d)i])$$

where

SBI_t = the proposed SBI value,
SBI_{t-1} = the existing SBI value,
p_t = the proposed price for rate element "i",
p_{t-1} = the existing price for rate element "i", and
d = the base period demand for rate element "i".

(e) An upper limit shall be established for each service category or subcategory pursuant to the following methodology:

$SBILimit_t = SBILimit_{t-1} * (1 + \Delta Z/RCAP) * (1 + GDP\text{-}PI - X) * (1 + f)$

where

$SBILimit_t$	=	the new PCI value,
$SBILimit_{t-1}$	=	the immediately preceding PCI value,
ΔZ	=	the dollar effect of current regulatory changes when compared to the regulations in effect at the time the PCI was updated to PCI_{t-1}, measured at base period level of operations,
RCAP	=	$(PCI_{t-1} / API_{t-1}) * R_{t-1}$,
API_{t-1}	=	the existing API value,
R_{t-1}	=	base period quantities for each rate element "i", multiplied by the existing price for each rate element "i",
GDP-PI	=	the percentage change in the GDP-PI between the quarter ending six months prior to the effective date of the new annual tariff and the corresponding quarter of the previous year,
X	=	productivity factor of 4.0%, or 4.7%, or 5.3% is the carrier so elects, and
f	=	the annual increase allowed relative to the exogenous, inflation, and productivity change in that service category.

(g) Local Exchange Carriers -- Service Categories and Subcategories

(1) The SBI limit for the common line service category shall limit the upward pricing flexibility for this service category to zero percent.

(2) The SBI limit for the common line density zone subcategories shall limit the upward pricing flexibility for these subcategories to ten percent.

(3) The SBI limit for the local switching density zone service categories shall limit the upward pricing flexibility for these service categories to ten percent.

(4) The SBI limit for the transport and tandem switching density zone service categories shall limit the upward pricing flexibility for these service categories to ten percent.

(5) The SBI limit for the database and other service category shall limit the upward pricing flexibility for that service category to ten percent.

USTA's Basket Proposal

- USTA's basket structure proposal provides no increased revenue and does not provide any unauthorized ability to shift revenues between access categories.

- Price cap companies need some limited flexibility to shift revenues between access categories.

  - To align access prices with unbundled network element prices.

Chart 1

- USTA's proposed formula is merely an algebraic restatement of the current FCC formula and produces identical results.

  - $PCI_{t-1} * \left(1 + \frac{\Delta Z}{R}\right) * (1 + GDPPI - X) = PCI_{t-1} * \left(1 + \left(\frac{R + \Delta Z}{R}\right)(GDPPI - X) + \frac{\Delta Z}{R}\right)$
  - New Formula = Current Formula

CHART 1

USTA's Restatement of the PCI Formula Produces the Same Result as the Existing PCI Formula

Ln#	Description	Abbrev.	Source	Common Line	Traffic Sensitive	Trunking
1.01	GDP-PI	GDPPI	1996 Annual Filing	2.6514%	2.6514%	2.6514%
1.02	Productivity Factor (X)	X	1996 Annual Filing	5.30%	5.30%	5.30%
1.03	Delta Z	Z	1996 Annual Filing	467,000	293,396	322,568
1.04	R(t-1)	R(t-1)	1996 Annual Filing	11,786,072	9,306,347	10,590,973
1.05	W	W	[R(t-1) + Z] / R(t-1)	103.9623%	103.1526%	103.0457%
1.06	Existing PCI	PCI(t-1)	1996 Annual Filing Proposed PCI	93.7772%	85.1215%	85.9023%
1.07	FCC Proposed PCI		PCI(t-1)*[1+W*[GDPPI-X]+Z/R(t-1)]	94.9107%	85.4795%	86.1741%
1.08	USTA Proposed PCI		PCI(t-1)*[1+GDPPI-X]*[1+Z/R(t-1)]	94.9107%	85.4795%	86.1741%

Chart 2

- The FCC needs to replace the "R" component in the PCI formula with a "RCAP" component.
  - $RCAP = \left(\frac{PCI_{t-1}}{API_{t-1}}\right) * R_{t-1}$
  - PCI adjustments should be made based on capped revenues and not be driven by actual pricing decisions.

- The FCC has already recognized this need in the existing Carrier Common Line formula.
  - Use of CCL capped rates at last PCI update in calculation of proposed Carrier Common Line rate cap.

Chart 2, cont'd

- Use of capped revenue needs to be incorporated into all PCI formulas through the use of an RCAP.
  - This merely corrects an oversight in the current rules.

- Impact is dependent upon current headroom and direction of exogenous change.

Example 1

PCI_{t-1}	=	100%	
API_{t-1}	=	50%	
R_{t-1}	=	$50	
Max Rev	=	$100	
Exog	=	$6	
PCI	=	112%	{100%*[1+(6/50)]}
Max Rev	=	$112	

Example 2

PCI_{t-1}	=	100%	
API_{t-1}	=	90%	
R_{t-1}	=	$90	
Max Rev	=	$100	
Exog	=	-$10	
PCI_t	=	89%	{100%*[1+(-10/90)]}
Max Rev	=	$89	

CHART 2

The Impact of Changing the PCI Formula from R(t-1) to RCAP

Ln#	Description	Abbrev.	Source	Access Services	Common Line	Traffic Sensitive	Trunking
2.01	Existing PCI	PCI(t-1)	1996 Annual Filing Proposed PCI		93.7772%	85.1215%	85.9023%
2.02	Existing API	API(t-1)	1996 Annual Filing Proposed API		93.7772%	83.3292%	85.7651%
2.03	Existing Revenue	R(t-1)	1996 Annual Filing	31,683,392	11,786,072	9,306,347	10,590,973
2.04	RCAP	RCAP	[PCI(t-1) / API(t-1)] * R(t-1)	31,900,502	11,786,072	9,506,514	10,607,916
2.05	Existing PCI	PCI(t-1)	1996 Annual Filing Proposed PCI		93.7772%	85.1215%	85.9023%
2.06	Existing API	API(t-1)	1996 Annual Filing Proposed API		93.7772%	83.3292%	85.7651%
2.07	GDP-PI	GDPPI	1996 Annual Filing		2.6514%	2.6514%	2.6514%
2.08	Productivity Factor (X)	X	1996 Annual Filing		5.30%	5.30%	5.30%
			w\ a Postive Exogenous Change				
2.09	Delta Z	Z	1996 Annual Filing		467,000	293,396	322,568
2.10	Proposed PCI @ R	PCI(t)@R	PCI(t-1) * [1 + GPDPI - X] * [1 + Z/R(t-1)]		94.9107%	85.4795%	86.1741%
2.11	Proposed PCI @ RCAP	PCI(t)@RCAP	PCI(t-1) * [1 + GPDPI - X] * [1 + Z/RCAP]		94.9107%	85.4245%	86.1700%
2.12	Proposed Max Revenue @ R(t-1)		[PCI(t)@R / API(t-1)] * R(t-1)	**32,116,511**	11,928,537	9,546,493	10,641,481
2.13	Proposed Max Revenue @ RCAP		[PCI(t)@RCAP / API(t-1)] * R(t-1)	**32,109,866**	11,928,537	9,540,350	10,640,979
			w\ a Negative Exogenous Change				
2.14	Delta Z	Z	1996 Annual Filing * -1		(467,000)	(293,396)	(322,568)
2.15	Proposed PCI @ R	PCI(t)@R	PCI(t-1) * [1 + GPDPI - X] * [1 + Z/R(t-1)]		87.6761%	80.2545%	81.0801%
2.16	Proposed PCI @ RCAP	PCI(t)@RCAP	PCI(t-1) * [1 + GPDPI - X] * [1 + Z/RCAP]		87.6761%	80.3095%	81.0841%
2.17	Proposed Max Revenue @ R(t-1)		[PCI(t)@R / API(t-1)] * R(t-1)	**29,994,659**	11,019,275	8,962,956	10,012,428
2.18	Proposed Max Revenue @ RCAP		[PCI(t)@RCAP / API(t-1)] * R(t-1)	**30,001,304**	11,019,275	8,969,099	10,012,930

Chart 3

- Changing the current access baskets to service categories, under USTA's proposal, does not:
  - Create any additional revenue; or
  - Allow unauthorized shifting of revenues between access categories.
- This is only true when the RCAP mechanism is used in the PCI formulas.

Attachment A

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